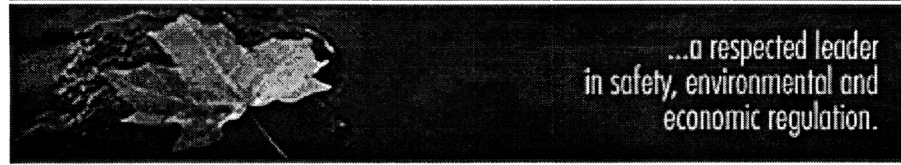


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Natural Gas Prices in Canada

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■ How are natural gas prices determined in Canada?

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How are natural gas prices determined in Canada?

The price that is paid by the end-users or consumers of natural gas is made up of the following components:

- a) the cost of the natural gas itself (for example, the price paid by local distribution companies for the gas it purchases on behalf of consumers). This is referred to as the "commodity" cost;
- b) the cost of transporting the gas through pipelines. This is referred to as the transportation or transmission cost; and
- c) the local distribution cost.

a) Natural Gas Commodity Cost

Natural gas commodity prices are negotiated between sellers and buyers of natural gas under various contract terms including length of contract and quantity. Some key factors which affect the commodity price include: supply, demand, storage levels in North American gas markets and taxes. Typically, prices increase during the winter months when demand is greater and decrease during the summer months when demand is lower.

Natural gas prices are also influenced by oil prices to the extent there is competition between oil and gas, particularly in some industrial and electricity generation markets (i.e. used as fuel to produce electricity). While oil prices are determined on the world market, and have increased significantly over the past few months. Natural gas prices are less influenced by developments outside North America.

b) Pipeline Transportation Cost

Pipeline transportation costs are the costs incurred in order to bring natural gas from the producing provinces to local distribution systems. These costs are made up of the tolls and tariffs that apply when transporting the gas through the pipelines. Interprovincial transportation tolls are determined by the pipeline company and must be approved by the National Energy Board.

c) Local Distribution Cost

Local distribution costs are the costs incurred to transport natural gas to customers or consumers through the local company's system. Distribution rates are usually established once a year, and are regulated at the provincial level (for more information please [contact your provincial regulator](#)).

Who regulates natural gas prices?

Natural gas "commodity" prices are **unregulated** and **vary according to prevailing market conditions**. While the prices negotiated between buyers and sellers are not regulated, the commodity price charged by a local distribution company or gas suppliers to its customers must be authorized at the provincial level.

The local distribution rates are regulated by provincial regulatory boards or commissions or directly by a provincial government. The provinces establish rates that are just and reasonable for each of the local distribution companies within a province.

Interprovincial and international pipeline transportation costs are regulated by the NEB and are determined through a public hearing process or through negotiations between pipeline companies and shippers. Even negotiated settlements must be approved by the NEB. The NEB ensures that pipeline tolls are just and reasonable and that there is no undue discrimination in services.

Why have natural gas prices increased recently?

In answering this question, it is helpful to remember which components of gas prices are paid by the consumer: the natural gas commodity cost, the pipeline transportation cost and the distribution cost. For the most part transportation and distribution costs are regulated by government agencies, and tend to change moderately over time. However, the commodity cost accounts for the bulk of the recent price increase experienced by consumers.

The natural gas market in North America is fully integrated (there is only one market, which covers the continent, as opposed to there being a number of individual local or regional markets). Therefore, commodity prices are determined on the open market by the forces of supply and demand; consequently, prices can fluctuate.

Other key factors affecting recent natural gas demand and in turn prices, include weather and the availability of alternate fuel sources in key market areas. Lately, colder than normal weather has been experienced across much of Eastern Canada and the northern United States. This combined with recent high crude oil prices has resulted in sustained high demand for natural gas and an increase in the natural gas commodity price. Recent world events leading to further uncertainty in energy supply has also contributed to higher prices.

While gas drilling has increased recently, it may take some time for new supply to be brought to the market and for consumers to see an accompanying decrease in price. As natural gas storage levels are drawn down to extremely low levels in Canada and the U.S. to meet the current high demand, we will see an increase in the summer re-fill requirement which may result in higher than average prices during this summer and into the next heating season. The actual price level however, will be dependent on alternate fuel prices and availability.

Gas users do have some option of utilizing alternative fuels or to reduce consumption when prices rise. Large industrial customers and some fossil fuel-fired electricity generating plants may have the ability to switch to alternative fuels. Residential consumers, on the other hand are more limited in near-term alternatives, apart from reducing consumption, as they are restricted by installed fixtures (furnaces, hot-water heaters, appliances).

How long will the current situation last?

In the near term (within the next year), prices will be highly weather-dependent. Natural gas demand is strongly affected by cold weather in winter, which boosts demand for heating, and hot weather in summer, which influences demand for electricity generation used for air conditioning. At this point, even if we experienced moderate temperatures that would reduce heating demand and temper prices, the current low levels of natural gas in storage compared to average, will likely mean higher than average demand to replenish the natural gas storage this summer and result in higher than average natural gas prices.

The current natural gas market is also greatly influenced by world events and crude oil prices. Significant changes in crude oil supply and prices can have a corresponding effect on natural gas prices.

It is impossible to say exactly how long the current situation will persist as weather and world events are difficult to predict. The current high demand, higher-price environment will send strong signals to natural gas producers to develop new gas supplies and increase production. However, it takes some time to explore and develop new natural gas sources. It is expected that additional gas supplies will be developed and that, once this occurs, consumers can look to some easing of prices.

On what basis does the NEB authorize exports of natural gas?

In the mid-1980s, the federal and provincial governments agreed to de-regulate the natural gas market thereby creating a free market for transactions. As a part of this agreement, the NEB was asked to implement a method for assessing applications for export licences that was consistent with the new policy framework.

Following a public hearing, the NEB implemented the Market-Based Procedure (MBP) to assess the merits of an application before granting a gas export licence. The MBP is founded on the premise that the marketplace will generally operate in such a way that Canadian requirements for natural gas will be met at fair market prices. The main premise of the MBP is that interested Canadian natural gas buyers have the opportunity to purchase natural gas on similar terms and conditions as the proposed export sales; if such an opportunity has not been provided, Canadian natural gas buyers may complain to the NEB prior to the export taking place.

For more information on the federal government policy regarding natural gas exports please see www2.nrcan.gc.ca/es/erb/english/View.asp?x=117.

Appendix A

Board Publications on Natural Gas

- Short-term Natural Gas Deliverability from the Western Canada Sedimentary Basin 2000-2002 (December 2000) ([Adobe Acrobat pdf format - 1206Kb](#))
- Canadian Natural Gas Market: Dynamics and Pricing (November 2000) ([Adobe Acrobat pdf format - 1598Kb](#))
- North American Natural Gas Liquids Pricing and Convergence (May 2001) ([Adobe Acrobat pdf format - 1403Kb](#))

Appendix B

Monthly Statistics on Natural Gas

- [Natural Gas Exports](#)
 - [Natural Gas Imports](#)
 - [Natural Gas Liquids](#)
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